



Technical Director
Financial Accounting Standards Board
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22nd September 2021

Via email: director@fasb.org, File Reference No.2021-004

Dear Technical Director,

Subject: Invitation to Comment, Agenda Consultation

The International Corporate Governance Network (ICGN) is pleased to respond to the Financial Accounting Standards Board's (FASB) Invitation to Comment (ITC) Agenda Consultation.

Led by investors responsible for assets under management of in excess of \$59 trillion, ICGN advances the highest standards of corporate governance and investor stewardship worldwide in pursuit of long-term value creation, contributing to healthy and sustainable economies, societies, and the environment. Our Members, including investors, companies, advisors and other stakeholders, are based in more than 40 countries, with over 30% based in North America.

ICGN offers an important investor perspective on corporate governance and stewardship to help inform public policy development and to encourage good practices by capital market participants as expressed through the ICGN Global Governance Principles (ICGN GGP) and other related policy documents. Transparent financial reporting is fundamental to good governance and investor protection and represents an ICGN policy priority. Reflecting this importance, recent revisions to Principle 7 on Corporate Reporting in the ICGN GGP, focus on corporate board responsibility for overseeing timely and relevant company disclosure for shareholders and relevant stakeholders relating to the company's financial position, approach to sustainability, performance, business model, strategy and long-term prospects.¹

Importance of Sustainability Reporting

We would like to begin our statement by placing emphasis on the importance of sustainability-related reporting to investors as part of transparent financial reporting. Investors have considerable interest in promoting high quality financial reporting-- addressing not only financial factors but also factors relating to a company's human capital and natural capital, including environmental, social and governance (ESG) or sustainability matters. This is increasingly relevant in both investment analysis and decision making, and in investor stewardship and company engagement. This is an opportunity for the FASB to show leadership by initiating

¹ ICGN Global Governance Principles.

https://www.icgn.org/sites/default/files/ICGN%20Global%20Governance%20Principles2021_0.pdf

projects to enhance transparency relating to sustainability. However, we do not see such projects presented in Appendix A of the ITC, and we would encourage the FASB, in consultation with the Securities and Exchange Commission (SEC) to address this as a priority. We expand on this point later in this letter.

Below, we provide our views in discussion form on specific issues and priorities for investors that arise in the ITC.

Priorities and investor focus

Most fundamentally we believe that the FASB should enhance its attention to understanding the needs of investors—who are most companies’ target audience as users of financial reporting. We note that the FASB has a broad agenda on reducing complexity and enhancing simplicity, which is positive. But there is not much focus on agenda items for investors. FASB’s stated mission is to “establish and improve financial accounting and reporting standards **to provide decision-useful information to investors and other users of financial reports.**”² This mission is vital to protect investors, as stated by FASB’s Chair Richard R. Jones, who said, “Investor perspectives are critical to the Board’s ability to develop effective standards, so we undertake a number of initiatives to proactively engage this stakeholder group in our standard-setting process.”³

Investors would like to see future projects that focus on providing benefits in the form of more decision-useful information. We also urge the FASB to deprioritize those projects that are primarily focused on the requests of preparers and auditors and offer limited or no corresponding benefit to investors. We recommend that the Board prioritize work on three topics identified in the ITC as follows:

1. Sustainability
2. Intangibles
3. Reporting performance and cash flows

1. Sustainability

Investors have long been focused on sustainability and have urged financial reporting standard setters to develop standards that promote sustainability disclosures, especially concerning climate risk and human capital. Too often the response historically has been to dismiss the issues as non-financial and beyond the remit of the FASB or relevant only for “special interests.” This is not how ICGN’s members — the world’s leading institutional investors— approach sustainability reporting. This form of reporting is increasingly being used in investment decision

² What we Do: FASB

<https://www.accountingfoundation.org/jsp/Foundation/Page/FAFSectionPage&cid=1351027541293#:~:text=The%20mission%20of%20the%20FASB%20is%20to%20establish,to%20investors%20and%20other%20users%20of%20financial%20reports.>

³ [FASB Issues 2021 Investor Outreach Report](#), Media Advisory, August 25, 2021.

making, investor/company engagement and voting decisions. We believe it is critical that the FASB and other key standard setters appreciate this urgency.⁴

ICGN has advocated through public consultations for better accounting for climate risk and human capital in financial reporting.⁵ Effective projects would ensure that estimations, assumptions, judgments, and measurements are standardized in a way that climate risk is a consideration. We encourage ongoing efforts to link climate reporting to financial reporting through the profit and loss statement and the balance sheet. As you may be aware the International Accounting Standards Board (IASB) is already reviewing this issue.

While climate risk has received arguably the most attention, the linkage of fundamental human capital considerations, including workforce relations do not appear on the agenda in a sufficiently robust way. The Human Capital Management Coalition provides comments on what might be possible regarding human capital in terms of impacts on financial reporting. We urge the FASB to consider those comments. Investors would like to see the FASB use its technical expertise to support the evolution of U.S. reporting requirements in a direction that more thoughtfully includes what investors have focused on.

We have long urged standard setters to include sustainability as part of their own work priorities. The IFRS Foundation and the IASB have been moving in that direction and we encourage the FASB increase its own attention and leadership with regard to sustainability-related reporting. The IASB chair recently highlighted sustainability and intangibles as priorities in a September 6, 2021 Wall Street Journal article.⁶ IASB Chair Barckow underscored the IASB's support of the sustainability reporting agenda.

Our trustees are considering setting up [the International Sustainability Standards Board], a sister board to the IASB. It will be concerned with setting standards for sustainability-related financial disclosures. Now, you could say, 'Let them take care of ESG and concentrate on your core stuff.' But a message that we are also hearing very consistently from jurisdictions is you should not really separate the two domains, as they go hand in hand. It could very well mean we're tackling standards together from an ISSB and an IASB perspective.

⁴ International Financial Accounting of Accountants (IFAC) statement emphasising changing investor sentiment in the case of climate reporting: <https://www.ifac.org/knowledge-gateway/contributing-global-economy/discussion/corporate-reporting-climate-change-information-and-2021-reporting-cycle>

⁵ ICGN Comment Letter on IFRS Foundation's Consultation Paper on Sustainability Reporting, 21 December 2020: <https://www.icgn.org/sites/default/files/27.%20ICGN%20Letter%20to%20IFRS%20Foundation's%20Consultation%20Paper%20on%20Sustainability%20Reporting.pdf>

⁶ Mark Maurer, *The New Head of the International Accounting Standards Board Chair Outlines His Priorities*, Wall Street Journal, 2 September 2021

In sum, we would like to encourage both the FASB and the Securities and Exchange Commission (SEC) to tackle sustainability in a meaningful way to provide investors with the information they need. It is important that the FASB does its part and does not operate under the belief that all sustainability considerations belong outside of financial statements.

2. Intangible Assets (including Research and Development)

We recommend that the FASB add a project targeting accounting for development costs, which are generally incurred with the specific objective of creating a product that will generate future revenues. The FASB should consider going beyond just aligning with the guidance in International Accounting Standard (IAS) 38, *Intangible Assets* as referenced in the ITC. There is a greater need to capture firm value with more precision.

IASB Chair Barckow also stated that intangibles will be an IASB priority:

[I]ntangible assets [such as brands and patents] is a topic that has come up several times. Intangibles are growing in importance. Many jurisdictions have moved from a manufacturing world to a service-oriented world. The second reason I would cite is the growing gap between book value and market value for many service-oriented firms. Providing more clarity and transparency as to what is really driving a company's value would be helpful for a start.⁷

There is much work to do regarding intangibles. The ITC asks about a focus on software. Several commenters would like digital assets to be disclosed at fair value, and there is a general need to improve valuations for profit making assets produced internally. Again, we encourage action and attention to this matter.

3. Reporting Performance and Cash Flows

The ITC does a good job in making a case for the direct method. The sole roadblock appears to be the cost involved in preparers modifying their reporting systems. Presently, the indirect method hides basic operational information while the direct method is more investor friendly. Interestingly, the indirect method is the one that is used even when it is less beneficial to investors. Investors would like the greatest reasonable insight into company operations to be able to gauge future prospects. The direct method is more likely to provide such information. A project to close the information gap and provide better information to investors is needed.

⁷ What we Do: FASB

<https://www.accountingfoundation.org/jsp/Foundation/Page/FAFSectionPage&cid=1351027541293#:~:text=The%20mission%20of%20the%20FASB%20is%20to%20establish,to%20investors%20and%20other%20users%20of%20financial%20reports>

Other issues

Technical Agenda

We reviewed the Technical Agenda on Appendix A and struggle to find projects whose main thrust is to benefit investors. The projects are possibly unduly focused on reducing complexity and enhancing simplicity, which are legitimate concerns. But is not clear to us how the projects named are investor focussed or will be of benefit to investors – if nothing else this warrants a clearer explanation.

As you know, the mission of FASB involves providing decision-useful information to investors and other users of financial statements. The key question under examination is the level of input investors should have in determining what is decision-useful. The review of Appendix A reinforces the call for an enhanced focus on the needs of investors which could come by possibly dropping certain projects that do not benefit investors in favor of those that have clear investor support.

Disaggregation

The discussion regarding disaggregation (including sustainability), intangibles and cash flows, offers promise for future projects, but we note that these important topics have been raised previously without meaningful projects pursued to address investor interests. Often this happens after the cost benefit analysis is applied. While the costs related to preparer and auditor concerns may be easier to quantify, they must be appropriately balanced against the full benefit to investors. What is at stake is nothing short of the proper allocation of capital. We strongly encourage the FASB to value such transparency in reporting and resist advocacy from those that want to reduce it—harming both investors as well as certain companies that have welcome transparency in their reporting. We applaud that investor issues have been identified in the ITC, but we hope that some of these reach the final work plan.

Chapter 3

We would prefer that FASB refrain from using capacity on any of the issues in Chapter 3. Chapter 3 focuses on reducing unnecessary transparency in current U.S. GAAP. None of the suggested topics directly support the interests of investors. We would envision that staff capacity would be allocated to projects that benefit investors, in relation to the mission.

KPIs

Management is in the best position to determine the drivers of value or KPIs. It is important to identify, quantify, measure and disclose such drivers of value. Otherwise, management keeps the information to itself and enhances the information gap with investors. It is important that investors receive more KPI related information in mandatory regulatory reports.

Government Grants

Investors would have benefited from standards regarding government grants during the pandemic. The need remains. The FASB should initiate a project that would provide investors the best information on the future prospects of the company in light of certain government grants.

We hope that our comments are helpful, and we look forward to engaging with you in this or other matters where we could provide meaningful input. Should you wish to discuss our comments further, please contact me or George Dallas, ICGN's Policy Director, by email at george.dallas@icgn.org.

Yours faithfully,



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